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## **Brazilian recent economic development**

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## Introduction

Brazil is the largest South American country with the biggest population. Endowed with very abundant natural resources, Brazil is emerging as the most powerful country of the subcontinent and thus the leader of other countries in South America. Even if the country has been hit by several global and internal economic crises, its economy continued to grow at a rapid pace. The strength of Brazilian economy is largely due to the economic programs and policies adopted by President Cardoso in the 1990s and President “Lula” da Silva in the first decade of the XXI century.

The rise of Brazil has been one of the greatest economic successes of the last decade. Brazil belongs to the “exclusive group” of thirteen economies that reached sustained high growth (an average growth rate of 7 % or more for at least 25 years ) in the years after the World War II. Between 1950 and 1980 Brazil saw its major structural changes (industrialization, the construction of Brasilia, accelerated urbanization) and political disruption (the 1964 military coup). But in its economic strength Brazil is weak too. The weakness of the Brazilian economy might be related mostly to debts, both foreign and internal. Very remarkable is the lost decade of the 1980s when a sovereign debt crisis was followed by major macro crises including bouts of hyperinflation amid mediocre growth.

The combination of periods of huge economic vigor, followed by periods of recession and economic uncertainty, seems like to constrain Brazil in the limbo of the mid-power countries.

This paper will analyze the contradictory rise of the Brazilian economy in the past decade, with a particular stress on the 2007 world financial crisis and the path of recovery adopted by the Brazilian government which worked in the short-term, while it seems not anymore profitable in the long-run. Now the country is facing stagnant GDP growth, as if the lucky star of Brazil was just a double-quick meteor.

Before talking about the contemporary monetary policy of Brazil, it would be useful start by doing a brief summary of the history of the Brazilian economy.

# CHAPTER ONE

## The Brazilian economy, 1950 to 2000

The period which we are going to analyze can be ideally started in 1964, the year of the beginning of the dictatorship; we will then deal with the difficult years of rebuilding democracy, the Real plan; follow by the election and the first mandate of President Lula. Historians use to call the years of the dictatorship the years of “military republic”. It might sound like an oxymoron but it is due to the preservation of the democratic institution made by the regime during that time . The military government believed that economic development was the only thing capable to bring Brazil in the international scenery as a bargaining power and it was possible only by restoring the process of import substitution. Therefore, the main thrust of the regime’s economic policy was to entrust less on the exportation of primary goods and to chase economic growth by increasing the production of manufactured goods, such as consumer durable goods, for the domestic and foreign markets. The process of import-substitution had been very intense in Brazil already from the aftermath of the World War II. It was firstly introduced with the consensus of the ECLAC (Economic Commission for Latin America and the Caribbean), under the guidance of Raul Prebisch <sup>1</sup>.

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<sup>1</sup> Professor of political economics at the Buenos Aires Nacional University. From 1930 to 1943 worked in the Banco Nación and then in the Ministry of Finance of Argentina. He was one of the founders and the first governor of the Central Bank of Argentina. From 1950 to 1963 Prebisch was Executive Secretary of the United Nation Commission for Latin America and the Caribbean (ECLAC), and later became Secretary-general of the United Nation Conference of Trade and Development (UNCTAD). (source: www.eclac.org)

During that time Brazil exported few number of agricultural products. The lack of strong value currency (US dollar), needed to buy good from the rest of the world, pushed Brazil to adopt the import-substitution strategy which would be able to reduce the impact of external shocks on the domestic economy. According to this strategy, those imports considered essential were set in at a favored interest rate, whereas imports of those goods that could be supplied with domestic goods were brought in at a high interest rate. At the same time some exports were stimulated with a higher interest rate in comparison with those of traditional exports.

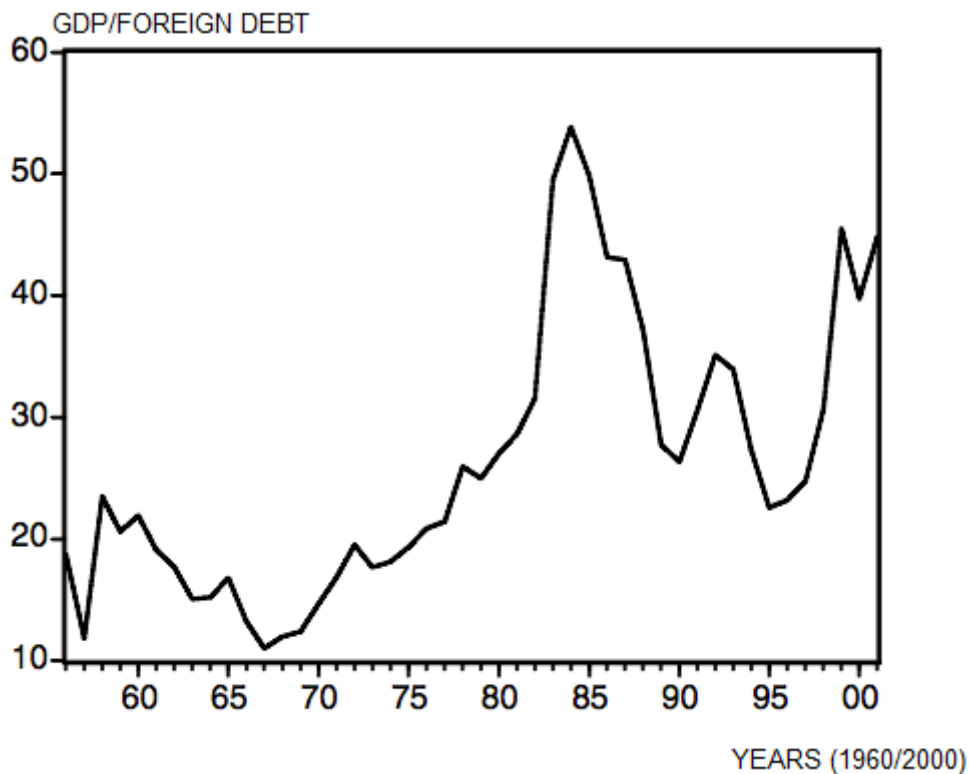
For the same aim the government introduced many complementary measures too, as the imposition of a tariff law to increase and solidify the protection of domestic industries and to offer inducements to direct foreign investment.

To facilitate the process of international borrowing the military government made a complete reorganization of the Brazilian financial system, to operate directly with the banking institution of United States. The government, in particular, passed a series of banking laws that allowed the Brazilian state and private firms to borrow directly from foreign banks and provided state guarantees for public and private companies that borrowed money from foreign banking institutions. As a result the current account balance recorded important surplus and cumulated international money as never before. At the same time the foreign debt increased fourfold, from 3.780 million (in terms of US dollars) in 1968 to 12.572 millions in 1973<sup>2</sup> (Figure 1), in parallel with the stream of foreign investment and foreign loans. The oil shock of 1973 stopped the trend whereas Brazil imported the 80% of its requirement.

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<sup>2</sup> World Development Indicators (2004). (data.worldbank.org)

Figure 1. Ratio of foreign debt on GDP



Source: Instituto de Pesquisa Economica Aplicada (IPEA), data available at [ipeadata.gov.br/ipeaweb.dll](http://ipeadata.gov.br/ipeaweb.dll).

To avoid the problem the regime decided to introduce a new plan of export substitution and started to use bioethanol ( produced from sugar canes) as an alternative to petrol. In 1979 the Brazilian Fiat produced the first bioethanol engine. But again the export displacement had to face with the world recession, and between 1974 and 1978 the balance sheet and the balance of payment were in deficit at all time. So that the government started to depend on foreign financial indebttness.

Like many other countries Brazil adopted a policy for growth based on foreign debt. Because of the rise of the price of crude oil in 1973, the producing countries had now a huge amount of money which was promptly put in the big European and American international banks. It follows that Brazil eagerly

took advantage of this situation and only borrowed capital from the newly-endowed banks in the United States and Western Europe.

Hence international banks reinvested this money in the developing countries, based on the belief that a State could never go bankrupt. For that reason they granted enormous loans in dollars, with variable interest rates, which were at 3% per year after discounting inflation. For the first time Brazil could avail itself large amount of foreign capital at low cost ready to be invested with no need of internal taxation and expenses policies in the short run<sup>3</sup>.

State-owned and private companies reinvested the same money with returns of between 20% and 25% per year, and the difference between the 3% paid as interest for the loans and the 25% earned by reinvesting that money stayed in the State. And this, it was thought, would have ensured the debt payment. Henceforth in 1979 the second oil shock occurred, which upset the entire world: the price of oil was 20 times higher as the one in 1973, and this brought a new surge of inflation. The same countries which had granted loans now were adopting restrictive monetary policies. As a result interests rates grew and this sharply increased Brazil's balance of payment and the size of the deficit. Interest payment soared while at the same time incomes from exports decreased. Nevertheless the military government persisted in borrowing, first of all to face an increasing debt burned, and it also tried to maintain the high-grow strategy. For that reason Brazil, like others countries of Latin America, tried to increase the volume of the exports, pushing down prices. Between 1978 and 1982 the balance of payment always showed deficits. Between 1981 and 1983 the GDP grew at the negative rate of an average of -2,4% per year. In contrast to bankers' assumption in 1982 Mexico defaulted on its foreign debt, prompting a sudden drying up on

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<sup>3</sup> According to the Ricardian equivalence theory, as reported in A. Aminghi, O. Blanchard, F. Giavazzi, *Macroeconomics: A European Perspective*, Bologna, il Mulino, 2011, p. 611-613,615, debt financing is essentially just future taxation. If a government issues a bond today to avoid raising taxes, it will need to raise taxes tomorrow to pay off the bond when it comes due. According to Ricardo's argument, it makes no difference to the public whether those increased taxes will come sooner (tax financing) or later (debt financing).



lending to all emerging markets. Brazil was forced to ask for the intervention of the IMF, essential to continue to service its foreign debt. For this reason Brazil and the IMF negotiated an austerity program conditional on the IMF lending.

When a country asks for a loan from the IMF the organization sends to the country a team of economic advisors to look at the nation-state economy and balance of payment problems. In order to see the loan accepted the country has to take some rigid economic policies to purchase one of the three tranches of credit. Using the IMF world itself: "Conditionality [is] understood as being the policies the Fund expects a member country to follow in order to be able to use the Fund's general resources."<sup>4</sup> As a result the IMF approval led also the country to re-obtain loans from international banks, because the IMF "seal of approval" ranks the a given state as a reasonable risk for the commercial banks of the developed countries. Of course conditionality depends on how much the state is requesting to borrow. In this case Brazil and the IMF agreed to several credit tranches to be issued between 1983 and 1985, under the condition that the Brazilian government: a) continued to devalue the Cruzeiro , b) cut domestic spending, c) froze all wages, d) reduced most of government subsidized credit, and finally e) curtailed credit to state-owned companies . Under those circumstances Brazil experienced a drop on its GDP, a rise in inflation and the decline in employment by the end of 1983. The debt crisis, the end of the "Brazilian economic miracle" with all its social consequences, which we are not going to analyze, led Brazil in 1985 to elect Tancredo Neves a president belonging to the opposition to the regime.

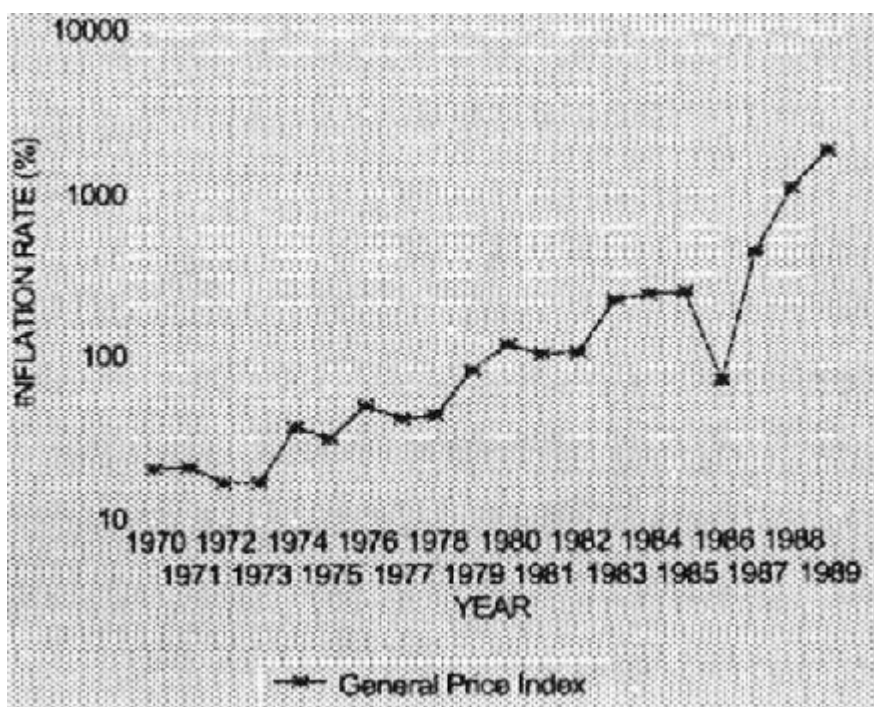
The second sub period that we are analyzing started with a very bad debt crisis which brought as a consequence a sharp increase in prices leading to hyperinflation. To bring inflation under control in 1986 the government adopted a new plan named *Plano Cruzado*. The plan took its name from the

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<sup>4</sup> IMF Articles of Agreements, Article V, section 3.

new currency introduced in that time, the Cruzado. It was in contrast with what the international organizations as the IMF and the World Bank dictated. So that the enforcement of the plan meant the complete breakage of the dialogue with the IMF and the freeze of the international credit. The plan lowered inflation but this brought the level of consumption to exceed the one of supply. As we can see in the figure below ( Figure 2 ), in 1989 inflation reached devastating levels, as big as 1800%<sup>5</sup>.

Figure 2. Annual inflation rate, 1970-1989



Source: IBGE 1990,1991

For that reason in the same year the new President passed a new plan, named as the president himself, “Plano Collor”, counted of monetary, fiscal and administrative policies with also exchange and import liberalization and privatization of public enterprises.

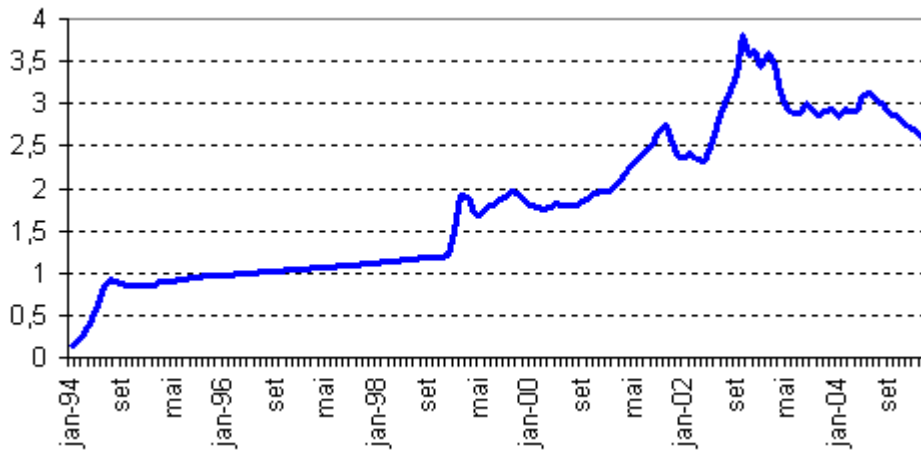
<sup>5</sup> IBGE 1990,1991.

Luckily the plan met the approval of the IMF and therefore the influx of foreign loans had resumed. Although the plan was not able to slow down inflation, and in 1990 Brazilian GDP lost around 4.3%. In 1992 the government tried to arrange a new plan which ended up being an abject failure.

In 1993 Cardoso was appointed Minister of Finance and in the same year he and his team worked out in a few months a plan of immediate action which provided for the reduction of the public expense and the abatement of tax evasion accounted for about 40 to 60 billions of dollar per year. This stabilization program had three stages: the introduction of an equilibrium budget mandated by the National Congress (Congreso Nacional), a process of general indexation (prices, wages, taxes, contracts, and financial assets) and the introduction of a new currency, the *Real*, pegged to the dollar.

In July 1994 Brazil implemented the most successful of its program to end inflation. The *Plano Real* was issued under the Washington Consensus, in other words it contained political economy measures dictated by the IMF and the World Bank, both located in Washington. These measures aimed to reduce the rate of inflation and restore the growth of the state economy through fiscal legislation, trade liberalization and privatization of public enterprises. The design of this plan is far different from the others because it did not depend on a general prices and wages freeze, but the strength of the plan was the de-indexation of the Brazilian economy. Prices and wages were converted in *reais* that began officially in par with the dollar. This exchange-rate policy had very important consequences for the domestic Brazilian economy. Expectations of a depreciation of the currency, coupled with the short-term stability of the exchange rate and a greater mobility of financial capital between Brazil and foreign financial markets led to a strong appreciation of the *Real* (Figure 3)

Figure 3. Dollar vs. Real (1994-2005)



Source: IPEA (Institute of Applied Economics Research), with data from the Central Bank of Brasil. ([www.ipeadata.gov.br](http://www.ipeadata.gov.br))

International enthusiasm for the Real Plan led to the restoration of money flows to Brazil, ensuring the government to maintain its policy of exchange-rate stability. The high level of capital flows to Brazil, more than financing the level of imports stimulated by the economic growth, lead to a sharp increase in Brazil's reserves of foreign currency. In 1995 finally the economy grew as much as 4.2%<sup>6</sup>. By the end of 1996 the program appeared to have succeeded in the goal of ending hyperinflation and economic instability.

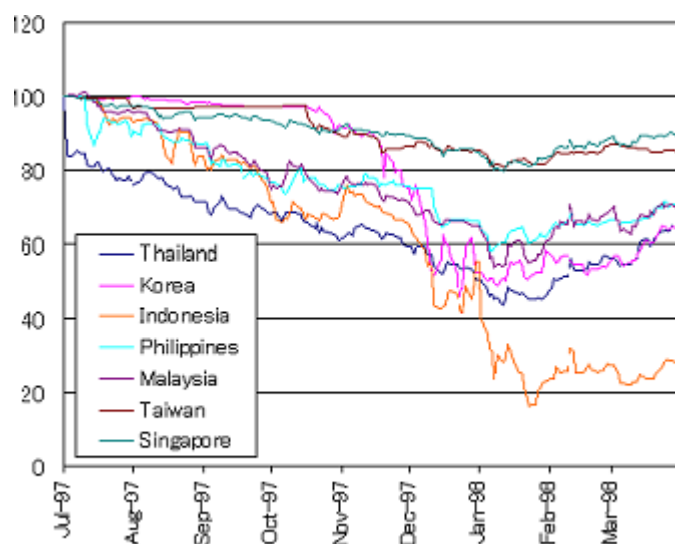
Although the improvements achieved in the short term are evident, the Real Plan did not solve the internal contradiction of the Brazilian economic system: a high fiscal deficit financed by foreign capital attracted by high interest rates. This situation created a dangerous vicious circle: to maintain fixed foreign exchange rates in order to pay for the deficit, high interest rates are required; the latter in turn worsen the fiscal deficit and so on.

The financial crisis in Southeast Asia and the one of Russia contributed to making the situation even worse. In fact in June 1997 some countries in

<sup>6</sup> World Development Indicators (World Bank) 2004.

Southeast Asia are forced to devalue their currencies. In a few weeks the Thai Baht, the Philippine Peso, the Ringgit of Malaysia and the Indonesian Rupiah lost 50-80% of their value against the dollar (Figure 4). The next “domino” to fall was Russia which suffered from an overvalued currency and a growing fiscal deficit. Russia tried to defend the currency with IMF support, but was ultimately forced to devalue the Ruble in 1998.

Figure 4. Collapsing currencies (Against US\$ - base year=1997)



Source: International Monetary Fund, IMF-Supported Programs in Indonesia, Korea, and Thailand: A Preliminary Assessment, January 1999.

The lack of confidence of international investors grew enormously to the extent that the capital flows to Brazil recorded a negative rate, which has not happened since 1990. The government as a last attempt to attract foreign capital started up the annual interest rate to 50%<sup>7</sup>, while the IMF, the World Bank together with the US government granted a loan for 41,5<sup>8</sup> billion of dollars. In 1999 to avoid the recession the government is forced to devalue the Real and put an end to the plan. Over the years the conditions did not

<sup>7</sup> International Monetary Fund (2006)

<sup>8</sup> International Monetary Fund (2006)

improve. In the two decades, between 1982 and 2002, Brazil was a key player in almost every major global financial crisis. In 2002, at the dawn of one of the most important elections in the history of Brazil, the Real still lost value and the foreign debt was equals to almost the 50% of the GDP (Table 1).

Table 1. External vulnerability indicators , 2000-2005

Indicators	2000	2001	2002	2003	2004	2005
Total Foreign Debt/GDP (%)	36.02	41.18	45.87	42.41	33.29	21.28
Net Foreign Debt/GDP (%)	28.41	31.92	35.88	29.79	22.43	12.69
Debt Service/GDP (%)	8.15	10.35	10.09	8.37	8.03	6.11
Debt Service/Exports (%)	89.08	90.64	76.80	58.07	50.32	41.14
Interest on Foreign Payments/GDP (%)	2.84	3.46	3.33	3.02	2.53	1.97
Current Transactions/GDP (%)	-4.02	-4.55	-1.66	0.82	1.94	1.78
International Reserves/ Total Foreign Debt (%)	15.22	17.08	17.95	22.94	26.29	31.75

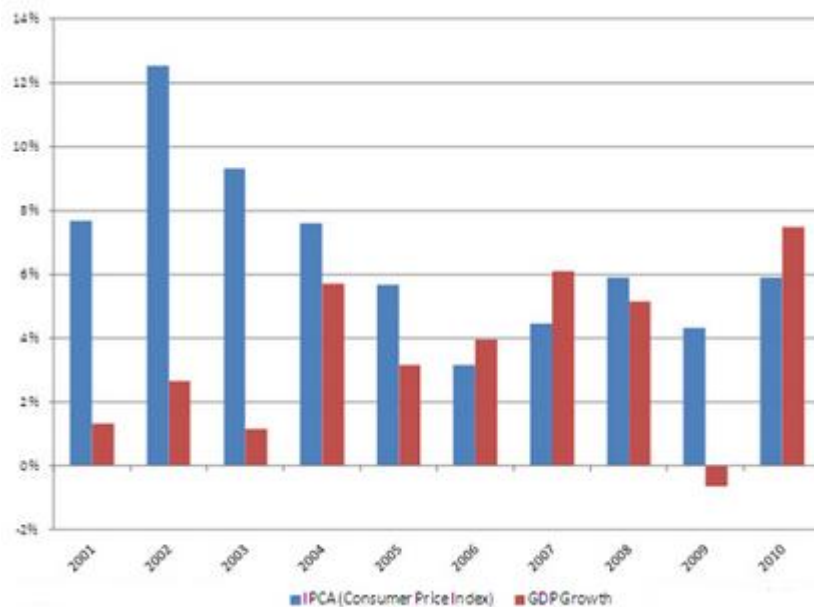
Source: Bacem, *Boletim do Banco Nacional do Brasil*, several edition

In October 2002 Luiz Inaciò “Lula” de Silva became Brazil’s President. Coming from the lower class, metalworker, his election signed for the first the victory of the voiceless people. He made his entrance into the political arena in the ‘70, when he had been a leader of the syndicalist movement. In 1980 he founded the first class party of Brazilian history, *Partido dos Trabalhadores*. His election had a great success at the international level. Although there were moments of disapproval he was re-elected in 2006.

During the first mandatory he focused the economic policy on the stabilization of the macroeconomics. The three main points of his action plan were: setting and inflation target through the variation of interest rates, a tight fiscal policy and the maintenance of floating exchange rates. The firsts results of Lula’s plan were exemplary: inflation under control thanks to interest rates set around 27% per year; a balance sheet surplus of 3% ( one point and a half

above the FMI requirement); more export and more production, that earned Brazil to an increase in GDP of about 5,9% in 2004 <sup>9</sup>(Figure 5).

Figure 5. Inflation and GDP growth (%), 2001-2010



Source: Central Bank of Brazil

An important thing to be underlined is the positive response on the foreign policy of President Lula, which made Brazil one of the main character of the international scene. In particular, his purpose to guide as a leader the poor countries by promoting the adoption of common positions and by hoping for tasks agreement in international negotiations, is fundamentally prominent. As a result he became the landmark of the weak economies of Mercosur. The Mercosur is a customs union signed in 1991 between Brazil, Argentina, Uruguay and Paraguay, in accordance with the Treaty of Asunción. The aim of the Union is the creation of a free trade area of people, goods and productive factors, through the gradual and automatic elimination of imports

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<sup>9</sup> Cental Bank of Brazil

barriers between the signatory countries and in addition by the practice of a common external tariff.

To summarize the results of the first mandate: economy grew, even if moderately; inflation went down from 12.5% in 2002 to 3.5% in 2006 (Figure 5); balance of payment in surplus and the country's vulnerability towards external debt fell. While the field of foreign policy was characterized by a determination to release Brazil from depending on U.S and European markets, through new and more intense commercial relations with countries with a similar stage of development, not only with the countries belonging in the Mercosur but also countries of Asia, Africa and the Middle East.



## CHAPTER TWO

### Brazil and the financial crisis

#### The re-election of President Lula

Luis Inciò “Lula” da Silva began his second term in office in January, 1st 2007. The President had reached the end of his first term with a strong popularity despite of a difficult year of constant corruption which placed him under investigation too.

He was expected to win in the first run, but in contradiction with the prediction, one of the challengers, Geraldo Alckmin, governor of Sao Paulo, belonging to the Party of Brazilian Social Democracy (from now PSDB), did quite well obtaining the 41.6%<sup>10</sup> of the votes against the Lula’s 48.6%<sup>11</sup> and so forcing the two candidates for the run-off. Alckmin was helped by a scandal which involved a member of the Worker’s Party (from now PT), which is known to be Lula’s party, offering to pay 1.7 million of reais (almost 800 millions of US dollars) for a dossier about Mr. Alckmin’s successor in Sao Paulo<sup>12</sup>. Auks Lula found the way to save the sinking ship by turning the inclination pro-business of the PSDB against itself. As a matter of fact Lula’s predecessor , President Cardoso, privatized electricity distribution, the telecoms company and the famous Companiha Vale do Rio Doce, Brazilian multinational diversified metals and mining corporation and one of the largest

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<sup>10</sup> Electoral Geography 2.0 *Brazil. Presidential election 2006*

<sup>11</sup> Ibidem

<sup>12</sup> Washington Post (online edition), *Alckmin Forces Runoff in Brazil Election*, Oct. 2<sup>nd</sup> 2006

logistics operators in Brazil<sup>13</sup>. Therefore joking with this trend to sell-off things, Lula suggested that the PSDB would sell parked cars on the street too. And this was crucial since Brazilians remembered that electricity privatization was hasty and incomplete, followed by many blackouts. The media fuss which arose hid the most important issues like the slow GDP growth, the debts which accounted the 40% of the taxes and the reform of the pension system. In addition it made him to be re-elected and guided Brazil through the difficult years of the crisis.

### **How the crisis affected Brazil**

Everyone knows the story of the 2007 financial crisis, how it spread from the real estate sector and soon infected the whole world economy. For that reason let us move on talking about how it bumped Brazilian economy.

Brazil managed the international financial crisis quite well, despite been severely hit at the beginning. The GDP went down by an average of 2.9%<sup>14</sup> at the end of 2008 and by 0.9%<sup>15</sup> in the first quarter of 2009 (Figure 7).

Although this may be true, it is also important to analyze that Brazil did better if compared with the developed countries and much better compared to countries as Russia and Mexico, at the same level in the developing field.

This fact can be explained in part looking at the pre-crisis conditions of Brazil, as it entered a vigorous growth cycle in 2006. Unlike Europe and the United States the domestic mortgage debt was very low. In addition the Central Bank of Brazil had implemented the regulation strongly since the banking crisis of 1990s. An important investment grades in 2008, the consolidation of the capital inflow and foreign exchange reserves, reaching 197 billions of US

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<sup>13</sup> Ibidem

<sup>14</sup> Central Bank of Brazil

<sup>15</sup> Ibidem

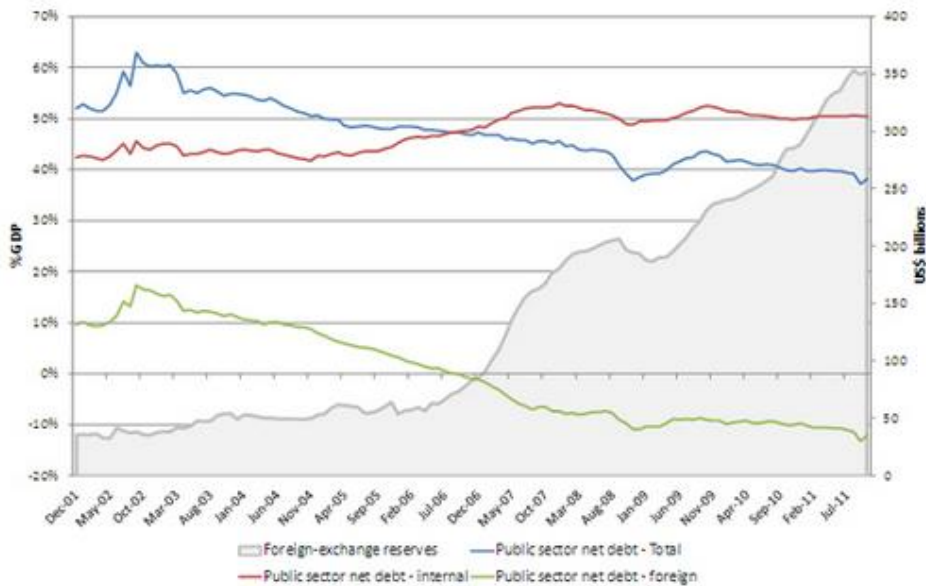
dollars in October of the same year. Foreign debt continued to fall, public debt was down and the National Treasury was no longer a debtor (Figure 8).

Figure 7. Brazil GDP Growth, 2007-2009



Source: Central Bank of Brazil

Figure 8. Debt foreign reserves



Source: The World Bank Group

The most difficult period to go through was undoubtedly the end of 2008, which affected particularly industry and saw a dramatic drop in the export of manufactured goods of about 37%<sup>16</sup>. The major problem was a sharp decline in sales to developing countries and in addition the cut of US dollars funding for export. The credit crunch affected also domestic market operation, so that companies had to cut their operation and start aggressive policies to reduce stocks. Because of a very bad cash flow situation, many companies were forced to reduce their production level and eliminate or prorogue investment projects. In most of the cases the stock liquidation resulted in enormous losses.

In order to estimate the extent of the downturn, it is important to remember that, even though the Brazilian economy began to recover in the second half of 2009, the foreshadow for industry stayed negative for the whole year estimating a decline of about 7.7%<sup>17</sup>. This trend was consolidated by several fiscal and monetary policies. The Central Bank of Brazil promptly furnished smaller banks with a big liquidity flow in order to give them strength and make them able to adjust their portfolio without and banks miscarrying. At the same time commercial credit in Us dollars was arranged, using foreign reserves, to provide liquidity for exporters. The Banco do Brasil played a key role in the operation. So that, the most important public banks, such as Banco do Brasil, Caixa Econômica Federal and Banco Nacional de Desenvolvimento Econômico e Social, expanded their loan portfolios significantly.

So, as said before, the Brazilian economy started the recovery in the second half of 2009. It is very important to stress on the fact that the perception of inflation, the eternal enemy during recession kept on falling. The indifference of institutions and the cautious monetary policy was consolidated by the

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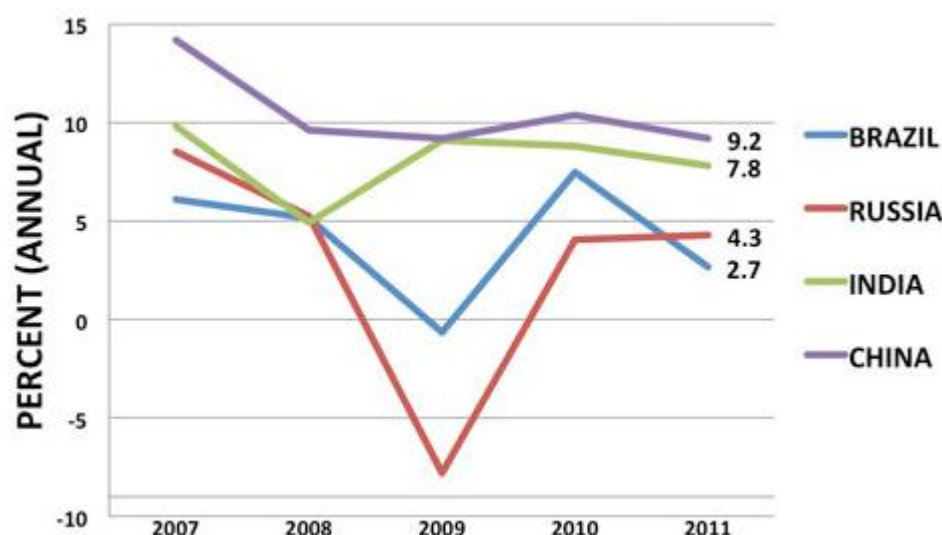
<sup>16</sup> IBGE (2010)

<sup>17</sup> Central Bank of Brazil

reevaluation of the Brazilian Real. Of course, the decision of keeping the inflation so low, fortified the demand for more credit, which accelerated throughout the years.

In parallel with consumer demand, Brazilian exports began to experience a positive knock-on effect from the strong recovery of the Chinese economy. After its GDP growth fell to 6% at the beginning of the year, the economy of the Asian giant, helped by its spectacular investment package, grew from 7.9%<sup>18</sup> to 8.95%<sup>19</sup> in the second and third quarter of 2009. Therefore, the exports of commodities recovered. In 2009 China became the largest trade partner of Brazil and was the destination for 13%<sup>20</sup> of national exports.

Figure. 8 GDP growth rate of BRIC's Nations



Source: The World Bank Group

At the same time, US participation fell to as low as 10%<sup>21</sup> putting the country on second place. The country came out quickly from the crisis and has been rewarded for this. The country risk measured by the CDS (Credit Default

<sup>18</sup> The World Bank

<sup>19</sup> Ibidem

<sup>20</sup> Central Bank of Brazil

<sup>21</sup> Ibidem

Swap) system<sup>22</sup>, was over 100 points ( currently the Italian CDS risk is about 229 points<sup>23</sup>). The São Paulo Stock Exchange index is the one with the greatest increase in value, in US dollars, among emerging countries. The Stock Exchange itself, which is a public company, is worth over US\$15 billion, the third largest in value worldwide, just behind Chicago and Hong Kong. The launch of Banco Santander (Brazil) shares was the most important in the emerging world in 2009<sup>24</sup>.

In the short term, another key point is the increase of the nominal public deficit to approximately 4.9%<sup>25</sup> in November 2009 from under 2% in October 2008. On the other hand, gross public debt (without discounting foreign reserves) rose from 53% in 2007 to nearly 65%.

On the other hand, during the currency crisis of 1998-99, the macroeconomic situation of Brazil was more fragile, both on the internal and on the external sides. The government was debtor on foreign currency and had a domestic primary deficit around 1% of GDP. In that situation, the government applied to the speculative attack against the Brazilian currency – that took place throughout the second semester of 1998 and result on the exchange rate devaluation in January 1999 – by requesting a loan from the IMF, as analyzed before, thus, adopting pro-cyclical (that is, restrictive) monetary and fiscal policies, which reinforced instead of alleviated the negative impact of the currency crisis.

In the midterm, the cost have been relatively heavy. Nevertheless, Brazil has shown that it belongs , together with China and India, to the group of countries that has best weathered the economic crisis. Moreover, from the international point of view, its influence has continued to grow during the

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<sup>22</sup> International Swaps and Derivatives Association. Due to the lack of regulation in the market for CDS, these instruments had been underwritten by almost any financial institution.

<sup>23</sup> Ibidem

<sup>24</sup> José Roberto Mendonça de Barros, *The Impact of the International Financial Crisis on Brazil (ARI)*, Dec. 4<sup>th</sup> 2010

<sup>25</sup> ECLAC, *Economic Survey of Latin America and the Caribbean s 2009-2010. Brazil*. p. 99-101

crisis, as can be seen from its active role in the G-20 and its not discuss regional leadership.

### **Brazil looking for regional leadership and beyond**

As may well be seen from the preceding pages, over the last years, under the guidance of President Lula, Brazil has moved into the international arena with the primary objective to reshape the international diplomatic and commercial geography in a more favorable way.

The main purpose of Lula was to make Brazil as a point of reference for the weak economies in an attempt to gradually reduce the influence of the United States, still strong despite the election victory of the Left party in almost all states in the area. But the venture taken by the President is by no means easy, since that despite having shown his appreciation for the victory of the *Izquierda* in many South American countries, Lula needs to tackle the dangers posed by the Venezuelan President Hugo Chávez, who seeks to steal from Brazil the ideological and economic lead role in the sub-continent. To maintain his major focus then the President has reinforced the international dialogue, showing the determination to make the developed countries hear the point of view of this Brazil which is trying to assert its weight even if just as a medium-power country. In doing that, very important to remember are the two agreements that Brazil has concluded with China-commercial- and Russia, which provides intensive cooperation on development of space programs. In addition remarkable are the utterances of President Lula in occasion of the 2008 G-20 summit of Washington in which he blames on Europe and the United States for the latter financial crisis<sup>26</sup>.

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<sup>26</sup> BBC News, *Brazil's Lula blames rich for crisis*, Sep. 13<sup>th</sup> 2009.

In that occasion Lula has criticized the lack of involvement of the United Nations on Iraq and he got that Brazil took over the command of the UN troops in Haiti, devastated by decades of civil war. The Brazilian government was well aware of the fact that the collaboration with the UN was important for the country, together with the favor of Russia and China, also in the view of the reform of the Security Council<sup>27</sup>. In fact Brazil set itself as the leader of those countries concerned to alter the composition of the Council and provide the allocation to other states of the status of permanent members.

Brazil has tried to get the role and the consideration as a regional leader implementing the report in the so-called South-South axis with bilateral agreements- such as the ones with China, for example, where trade has increased twelve-fold between 2001 and 2009 and with the entry into operation of the Tupi oil field in Brazil will become the first supplier of oil to Beijing; with regard to Iran, the attempt to build an axis together with Turkey to ease tensions U.S. against Tehran failed with the imposition of a fourth round of sanctions by the UN Security Council; finally, with countries like France and Russia, Brazil is deepening its trade relations and military cooperation- and multilateral agreements too like the more recent and already mentioned role in the G-20, in which Brazil is a member of the privileged forum for the discussion of international economic influence.

Interesting to be pointed out is the relationship with the United States of Lula's government which by reason of political preferences toward a rebalancing of the international distribution of the power, have been predictably thesis. But, for various reasons, there has been even more of a grounds for convergence. Regarding the points of divergence, these are

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<sup>27</sup> As stated by then President of Brazil Luis Inácio Lula da Silva at the General Debate of the 63rd Session of the United Nations General Assembly in September 23th, 2008: "The United Nations has spent 15 years discussing the reform of its Security Council. Today's structure has been frozen for six decades and does not relate to the challenges of today's world. Its distorted form of representation stands between us and the multilateral world to which we aspire. Therefore I am much encouraged by the General Assembly's decision to launch negotiations in the near future on the reform of the Security Council."



related to the anti-imperialist and anti-hegemonic of Lula and the PT. Noteworthy is the Brazilian belief that the current rules of finance and international trade penalize the country, jeopardizing the full development. In addition the dispute on the U.S import duty on Brazilian major exports, such as ethanol. With regard to the convergences crucial is shared desire for stability in Latin America and in the international context and the interest to contain the populist regime of Chàvez.

## CHAPTER THREE

### Contemporary Brazil

#### The end of the Lula era and the 2010 election

In December, 2010 the curtain finally went down for Luis Inaciò “Lula” da Silva. The meteoric rise of the former leader had completely smashed the traditional mould of Brazilian politics. But the leader, even if tried in body from cancer, did not seem to be ready to say goodbye to the political scene, since he himself was to decide the fate of the country designating as his successor his Chief of Staff, Dilma Roussef, and promoting her with all his media power. The popularity of the former president proved to be crucial in the 2010 election. Just six months before the polling day the candidate of the PT, Lula’s party, was almost unknown to the Brazilians, as she had never held elected office even as she worked closely with Lula ever since he was Minister of Energy and Mines, and later become the President’s Chief of Staff. Thanks to the support of the charismatic leader, Ms Roussef just had to avoid mistakes and mess during the campaign to ensure victory. Surprisingly she did not win in the first run, only to succeed in securing the 56,05%<sup>28</sup> of the

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<sup>28</sup> Electoral Geography 2.0, *Brazil. Presidential Election 2010*.

votes in the second run. Lula's protégée is the first female Brazilian president and won the largest election in the history of Latin America<sup>29</sup>.

As soon as she started her mandate in January 1<sup>st</sup>, she made clear immediately that she represented continuity with Lula's government. Moreover the electors were expecting nothing more than the continuation of Lula's policies with lower international profile and bigger focus on economic and domestic policies, and particularly a strong role of the state in strategic areas.

The essential elements of the Lula government have been maintained and reinforced with Rousseff. The economic model has undergone the same adjustments that Lula himself would have made, facing with the change in the global economy. The government also tried to manage to control inflation and the balance trade; this required interest rates adjustment and other instruments against excessive fluctuation or appreciation of the currency.

### **2010: the last of the great Brazil's growth years**

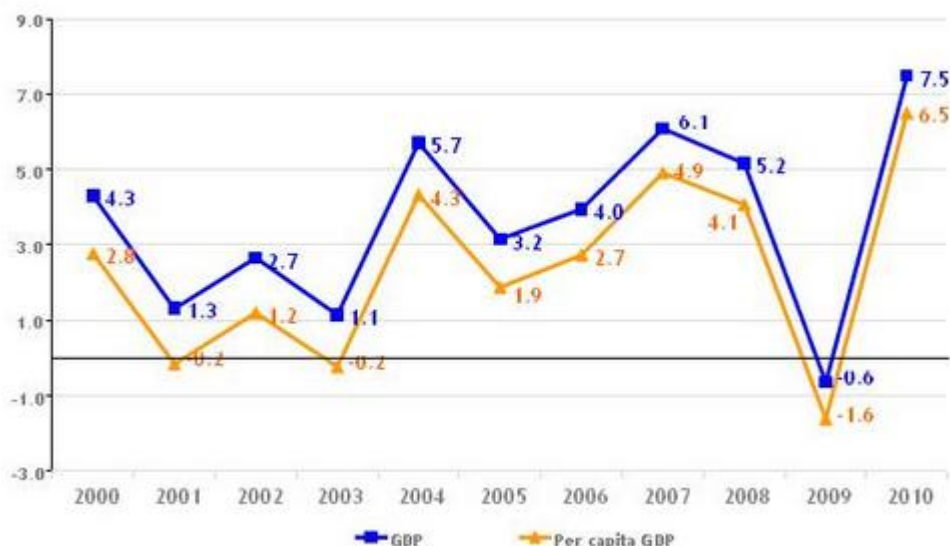
The solid economic performance during the financial crisis, the earlier recovery in comparison with the other developing and developed countries and the huge growth of 7,5%<sup>30</sup> in 2010 (Figure 8) – the fastest growth rate in the previous 25 years- led Brazil from being a regional power to being a global one. For the first time domestic consumption has become an important factor in Brazilian growth.

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<sup>29</sup> An estimated 135 million Brazilians up to 201 million went to the polls, almost the 79% of the whole population of Brazil. *Source: Electoral Geography 2.0, Brazil. Presidential Election 2010.*

<sup>30</sup> IBGE (2011)

Figure 8. GDP and GDP per capita (annual growth rate %)



Source: IBGE

The Central Bank's Monetary Policy Committee (Copom) discounted rate at 8.75%<sup>31</sup> in the first part of the year, then decided to increase it to 10,75%<sup>32</sup>. Brazil has always been generally open to foreign investment so that it is the largest recipient of foreign direct investment of Latin America and the United States are the first investors in the country. Even though, through the year, foreign exchange policy was aimed to prevent that more foreign currency liquidity would produce excessive volatility and imbalances in the exchange market. With this background the Central Bank maintained a policy of controlling international reserves. The real recorded a 4.31%<sup>33</sup> nominal appreciation against the US dollar in 2010. The demand of imported goods and services increased as a sign of the consolidation of the Brazil Economy recovery, with an impact on the current account deficit, which totaled 47.4<sup>34</sup>

<sup>31</sup> Central Bank of Brazil (2012), *2010 Annual Report*, p.43

<sup>32</sup> Ibidem

<sup>33</sup> Central Bank of Brazil (2012), *2010 Annual Report* p.88

<sup>34</sup> Ibidem, p.90

billion of US dollars in the year. Trade balance registered its tenth consecutive positive result with a surplus of 20.3<sup>35</sup> billion US dollars in 2010. In preparing for the 2016 Olympics in Rio the government is committed to invest billions of dollars in roads, airports, sport facilities and many other areas; as a consequence Brazil needs to keep attracting foreign investments. Export promotion was among the main components of the Rouseff plan to increase growth and reduce the country vulnerability to international financial market fluctuations. To do this the government sought access to foreign market through trade negotiation and increased export promotion, including no taxation for exporters.

In addition Brazil has been one of the leading players in the World Trade Organization's Doha Round negotiation. To increase the international profile the government administration expanded trade ties with developing countries. Between 2008 and 2010 with the Mercosur signing two important arrangements respectively with Iran and Egypt.

China increased its purchases of Brazilian soy, iron ore and steel and became Brazil's first export market and also one of the biggest sources of investment.

It is also important to recall the government program to reduce dependence on imported oil. Together with the United States, as the world's largest biofuel producers, Brazil worked on a memorandum of understanding how to make sustainable biofuel a global commodity. In March 2011, that memorandum was subsumed under the Strategic Energy Dialogue, a partnership announced by President Rouseff and President Barack Obama.

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<sup>35</sup> Ibidem, p.91

## From great to good: the year 2011

The Brazilian economy slowed in 2011, recording a GDP growth of just 2,7%<sub>36</sub> (the second lowest growth rate since 2003). This deceleration might be due to policy measures accounted to keep inflation below the target range( 6.5%) and to the difficult international situation.

In 2011, the foreign trade policy was aimed to the reinforcement of instruments for commercial protection and to the stimulation to innovation and national production, in order to increase the country's industrial competitiveness in both domestic and foreign markets.

In external sector export register an annual growth of 26.8%<sub>37</sub> while import increased the 24.5%<sub>38</sub> in 2011. This surplus helped to offset the services and income deficit. The 2011 account deficit was about 2.1%<sub>39</sub> of GDP. Foreign Direct Investment (FDI) global flows totaled 1.5 trillion of US dollars in 2011<sub>40</sub>, according to the Unctad preliminary estimates, rising 17% in the. FDI net inflows to Brazil reached a record of 66.7 billion of US dollars in 2011<sub>41</sub>, increasing 37.4% in the year.

As it can be easily understood this greater inflow of capital resulted in an appreciation of the exchange rate in August of the same year. The government's reaction was the introduction of measures to regulate capital inflows.

In the second half of 2011 the Rouseff administration deployed initiative to shore up manufacturing industry. Among these initiatives the Brazil Maior' plan is worth mentioning. Inspired by the US Buy American Act of 1933, the Brasil Maior' is a three-year plan thought to help stimulate Brazilian industrial

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<sup>36</sup> Central Bank of Brazil(2013), *Annual Report 2011*, p. 13

<sup>37</sup> Ibidem, p. 94

<sup>38</sup> Ibidem, p. 101

<sup>39</sup> Ibidem, p. 97

<sup>40</sup> Ibidem, p. 117

<sup>41</sup> Ibidem, p.118

sectors and cope with adverse competitive conditions and a strong local currency. The plan has eight pillars: foreign trade, investment, innovation, training and skills, sustainable production, competitiveness of small businesses, special actions on regional development and consumer welfare. At the beginning of 2011 the Central Bank of Brazil introduced a new prudential bank regulation with a stricter capital requirement for banks lending long-term.

The exchange rate policy in 2011 was aimed to contain the appreciation of the Real. In July the exchange rate dropped to 1.55 reals per 1 dollar. The Real appreciated 7% in real term during 2011. The situation changed in August when global uncertainty mounted and by December 2011 the exchange rate devaluated with a nominal rate of 1.87 reals per 1 dollar. Despite this exchange rates fluctuation (Figure 9) the Brazilian real depreciated 12.6% against the U.S. dollar in 2011<sup>42</sup>.

Figure 9. Exchange rate fluctuation 2011



Source: fx-exchange.com

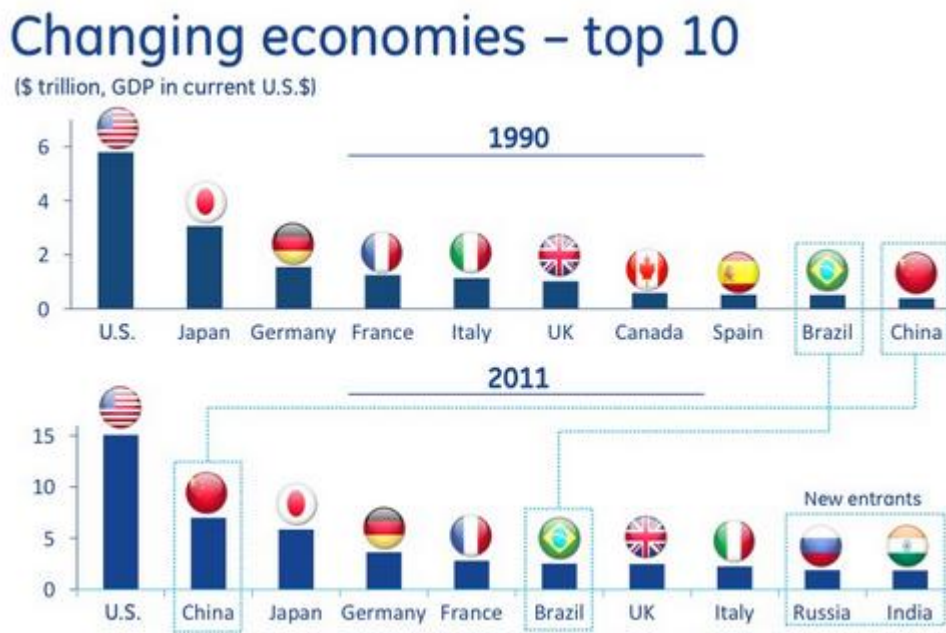
Above all it would be wrong to say the 2011 had been a bad year for Brazilian economy. In fact this is the year in which Brazil overtook United Kingdom as world's sixth largest economy. Despite the economic slowdown Brazil had been able to overpass Britain and take its ground in the ranking of the world's

<sup>42</sup> Central Bank of Brazil(2013), *Annual Report 2011*, p. 85

largest economies (Figure 10). For several months the two economies have been neck-to-neck. Britain has not experienced economic growth during the year 2011 but the pounds increased its value in comparison with the dollar, in contrast to the reais which had lost grounds. So the importance of currency movement to determinate the size of a country's economy. However in this case the growth of Brazilian economy, even if a modest one, was enough strong to let the country figure among the world's richest economies.

Anyway ,because of the particular strength of the British pounds, Brazil is not expected to hold on for long.

Figure 10. The world Largest Economies 1990 -2011



Sources: [www.businnesinsider.com](http://www.businnesinsider.com)



## The year 2012

In 2012 it was clear that Brazil was not the same growth machine it was just 3 years before. The country that well survived to the largest credit crisis ever in modern times was now growing less than the United States where the crisis took place. China was slowing and the Brazilian export were suffering. The GDP grew even slower than in 2011, recording a weak 0.9%<sup>43</sup> while the Minister of Finance, Guido Mantega, had been estimated a growth of 4 point percentage to calm down the general warning of banks and investors.

Brazil was now experiencing that the low interest and exchange rates they have always want to do never lead to economic growth, even in an emerging economy.

The slowdown was driven by both domestic and external factor. Foreign direct investment remains sufficient to cover the account deficit, which has reached around 2.2% of GDP<sup>44</sup>.

The Central Bank of Brazil in 2012 launched a program to secure long-term sustainable growth for the years 2012-2015 guaranteeing as much as 5.8 billion of US dollars to stimulate investment<sup>45</sup>.

When we said that the Brazilian surpass on Britain as the sixth richest economy will not hold on for long, we were right. In fact, in 2012 Brazil turn back in the seventh position, in contrast with what Minister Mantega predicted, saying that Brazil in 2012 would be able to overtake Germany and French too<sup>46</sup>.

The rate changing is mostly due to the strong devaluation of the Real that reduces the country's nominal GDP, and the Real has lost about 10% in 2012<sup>47</sup>. Nonetheless Brazil remained the seventh largest world economy

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<sup>43</sup> Central Bank of Brazil (2013)

<sup>44</sup> Ibidem

<sup>45</sup> [www.worldbank.com](http://www.worldbank.com) , *Brazil overview*, 2013

<sup>46</sup> BBC News, *Brazil loses ground again*, 26 December 2012.

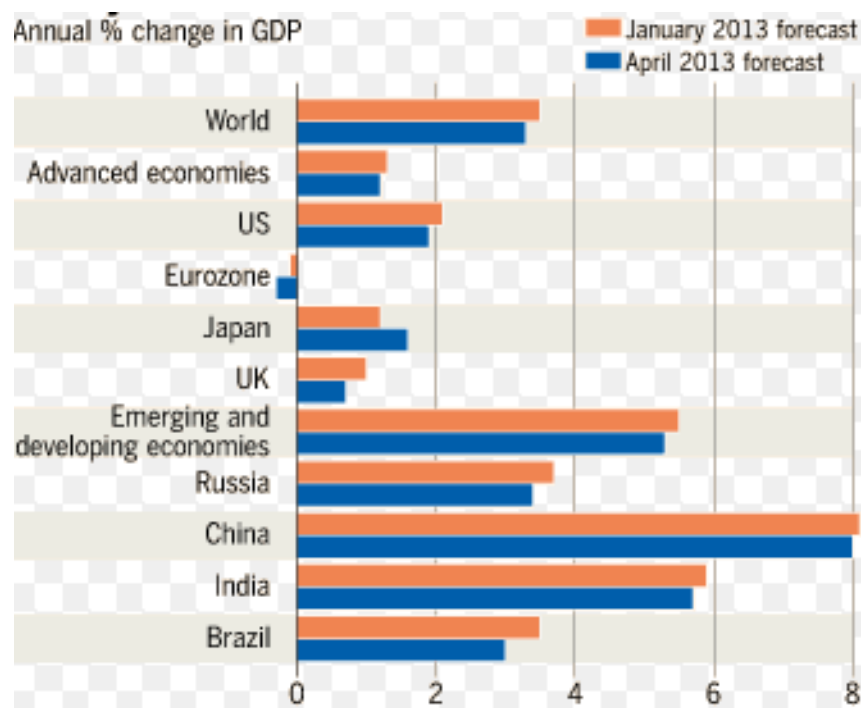
<sup>47</sup> Central Bank of Brazil (2013)

above the United Kingdom and Russia, and immediately followed by Germany, French and, only in the tenth position, Italy.

In the exports field, basic interest rates have been systematically reduced to 7,25%<sup>48</sup> at that time. This was used as an expedient to alleviate the country's debt pains and to encourage investment in the real economy. In 2012 the rate of investment amounted to about 18%<sup>49</sup> of GDP, with China investing almost 50% and India more than 30% of their GDP.

Most analysts expect a recovery of the Brazilian economy in 2013, forecasting growth rates between 3% and 4% (Figure11).

Figure 11. GDP forecast growth for 2013 (IMF)



Source: IMF

<sup>48</sup> [www.worldbank.com](http://www.worldbank.com) , *Brazil overview 2012*

<sup>49</sup> Ibidem

## **2013 World economy outlook**

According to the IMF World Economy Outlook (April 2013) global growth is staying above 3%, the same as 2012. This is driven by weak domestic demands and slower growth in emerging market economies as well as by more recession in the Euro area.

Emerging market economies have been hit hardest, because of the recent increase in advanced economy interest rates and more price volatility, which, plus a weaker domestic activity, lead to capital outflows and currency depreciation.

The global underperformance could be linked to three main reasons: first the continuing growth disappointment in emerging market economies; secondly to the deeper recession in the Euro area which exacerbate the effects of growth and the impact of tight fiscal and financial condition; and at third the United States economy expansion at a weaker pace. On the other hand growth is being stronger than expected in Japan.

The World economy is expected to better in 2014 with a growth forecasting of 3,75%<sup>50</sup>.

## **2013 Brazilian economy forecast**

It is not easy to collect data and to do a complete profile of the Brazilian economy of the current year.

As we said before in 2012 the economy grew just 0.9% and this let the Brazilian media to coin a new word "*Pibinho*" which means "little GDP".

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<sup>50</sup> IMF (2013)

Now the economy looks like recovering thanks to a boom in agriculture. Analysts believe that Brazil, together with the other BRIC's countries, are now moving to a period of lower but constant growth, which means that Brazil should close the year with a growth rate near to the one of 2011 (2.7%).

Furthermore Brazil's economy grew by 3.3% in the second quarter of 2013, compared with the same quarter in 2012. In addition the IBGE (Istituto Brasileiro de Geografia e Estatística) said also that Brazil grew by 1.5% in the first quarter, more than the expected 0.9%.

Moreover the Minister Mantega reduced the growth target announced for 2013 from 3% to 2.5%, and the one for 2014 from 4.5% to 4%. The second quarter of the present year was good also for the foreign exchange rate with the Real gaining 0.8% to the US dollar. Whereas this is an inconsistent recovery since the Real has lost the 20% of its value from the beginning of the year. As a consequence the capital inflow slowed. The fall of the Brazilian Real stoked inflation, currently at 6,15%

The Copom (Central Bank's Monetary Policy Committee) increased the interest rate by half a percentage. The higher interest rate, now at 9% (August 2013), would help, according to the IMF, to control inflation and increase investor's confidence.

In September 27<sup>th</sup> of the current year the IMF Representative for Brazil Paulo Nogueira Batista, at a business seminar in Sao Paulo, said that Brazil has got a solid economy. The IMF Executive director noticed signs of recovery in the economy and argued that the recent speculation on Brazil's economy is exaggerated, blaming mostly on recent publications of the famous British publication *The Economist*<sup>51</sup> and of the American *Financial Times*<sup>52</sup>.

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<sup>51</sup> "The Economist", print edition, September 2013, *Has Brazil blown it? A stagnant economy, a bloated state and mass protests mean Dilma Rousseff must change course.*

<sup>52</sup> In particular Mr. Nogueira Batista refers to some articles published in 2012 which wondered whether Brazil's economy had failed and why the markets do not trust Ms Rousseff referring to the Brazilian president as too interfering.

The IMF official showed that fiscal fundamental of Brazilian economy are strong, unemployment is decreasing and monetary policy is working as well. In addition, according to what Mr. Batista said , financial system regulation is good, end reserves as well as foreign direct investment are high.

A new Financial Stability Report from the Central Bank of Brazil echoes Batista's point of view. It covers the first half of the year and underlines Brazilian resistance to external shocks, like the slowdown of Chinese economy. Despite the volatile global market, according to the Financial Stability Report, Brazil fared relatively well.

However the IMF Representative warned Brazil against the current account deficit, which in the first part of the year was bigger than the total one of 2012. According to the bank's report the Brazilian banking system's solvency is at an average of 16,9%, above the required 11% of minimum.

On the other hand it has to be said that the external scenario worsens the projection on Brazil's future. Recently the US Federal Reserve decided to reduce its monthly purchases of bonds to stimulate the economy. Brazil, together with other four countries (Indonesia, South Africa, Turkey and India) belonging to the group of the so called "fragile five"<sup>53</sup> , will risk a lot when FED Chairman, Mr. Bernanke, will make the inevitable announcement to cut his balance-sheet expansion. About that, the former President Cardoso and E. G. da Fonseca, professor at Insper Business School, said at an event sponsored by non-profit group IDS that the success of Brazil depends on the intensity of the FED's tapering which will probably take place in January 2014.

In addition all the five countries will have election next year, and it is well known that political uncertainty troubles the market and worsens the investors. In particular, the case of Brazil is quite alarming after the popular protests that took place during the last years. Because of that, President Roussef approval ratings fell from 57% to 30%<sup>54</sup>.

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<sup>53</sup> Morgan Stanley, 2013.

<sup>54</sup> IBGE, August 2013.

To conclude even more important for Brazil is maybe the future of Chinese economy. Currently the Chinese Central Bank (PBOC) dealt with a market's generalized fall and banks' crash. This will effect Brazil since generally Brazilian commodities prices follow the Chinese growth.

## Conclusion

Passing through the history of Brazilian modern economy we have seen that from the second half of the XX century, more precisely from the rise of the dictatorship in 1964, economic development has always been the heart of the country's policies in order to put Brazil in the international scenery as a bargaining power. To achieve this goal the Brazilian government adopted several measures throughout the years.

In the period of the military regime the way used to improve the country's economic development was the process of import substitution. So the government trusted less on the exports of primary goods and increased the production of manufactured durable goods. In addition, the regime substituted the imports of those goods that could be easily replaced with domestic goods, in order to stimulate internal industry and reduce exports. At the same time it started to protect domestic industries and to attract foreign direct investment. With the oil shock of 1973, since Brazil imported the 80% of its oil requirement, the country, according to the import substitution strategy, began to produce bioethanol, a valid substitute of crude oil made up from sugar canes. The world's recession between 1974 and 1978 sharply affected Brazilian economy and the government to avoid recession and to sustain economic growth started to depend on foreign financial debt. Brazil started to borrow money from those country that, because of the oil production, were now well-disposed in lending money to countries, believing that a State could never go bankrupt. With the second oil shock in 1979 the same countries which had granted loans to Brazil were now asking for more interest rates and adopting restrictive monetary policy. This increased Brazil's balance of payment and the size of the deficit. As a result interest payment soared and incomes from exports decreased. Regardless the government went on borrowing to face the increasing debt and to maintain the high-growth

strategy. In addition Brazil tried to increase the volume of export by cutting down prices.

In 1982 Mexico declared insolvency on its foreign debt and it meant an immediate drying up on lending to all emerging market. To pay its foreign debt Brazil asked for a loan from the IMF in 1983, with the following period of austerity which was necessary to fulfill the IMF's conditionality clauses. Under those circumstances Brazil experienced a drop on its GDP, a rise in inflation and a decline in employment by the end of 1983. The end of the Brazilian economic miracle led to the overthrow of the military regime in 1985 and of the economic policies too. In fact the new democratic government to enforce economic development adopted in 1984 a new plan, *Plano Cruzado*, introducing a new currency, the Cruzado. Since it was in contrast with IMF's and World Bank's guidelines the enforcement of the plan meant the complete breakage of the dialogue with those organizations and the freeze of the international credit. However in the short run the plan succeeded in cutting down inflation but by the end of 1989 it reached devastating levels, as big as 1800%<sup>55</sup>. In the same year the new government passed a new plan, named as the President of Brazil, "Plano Collor", made up of monetary, fiscal and administrative policies with also exchange and import liberalization and privatization of public enterprises. This plan met the favor of the IMF, the credit was restored but was not able to slow inflation and the GDP continued to go down. In 1993 the new Minister of Finance Cardoso worked out a plan of immediate action which counted three stages: the introduction of an equilibrium budget mandated by the National Congress, a process of general indexation and the introduction of a new currency, the Real, pegged to the dollar. Issued under the Washington Consensus, it was the most successful Brazilian plan to reduce inflation. The international enthusiasm for the new currency led to the restoration of money flows to Brazil and in 1995 finally the

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<sup>55</sup> IBGE 1990,1991.



economy started to grow again. But the Asian financial crisis of 1997 worsened the situation and after the devaluation of the Thai Baht, the Philippine Peso, the Ringgit of Malaysia, the Indonesian Rupiah and the Russian Ruble, in 1999 Brazil was forced to devalue the Real and put an end to the *Plano Real*. Neither a loan of 41,5 billion of dollars provided by the IMF, the World Bank and the United States, nor the last attempt of the government to attract foreign capital starting up the annual interest rate to 50%<sup>56</sup>, helped Brazil avoid recession. With the election of Luis Inácio “Lula” da Silva in 2002, Brazil started to shine again. The aim of President Lula was to stabilize the macroeconomic background of Brazil. The results of his strategy were immediately evident: inflation under control, balance sheet surplus, more exports and more production, that earned Brazil to an increase in GDP of about 5,9%<sup>57</sup> in 2004. It was the beginning of a period of steady growth which, excluding the 2009, goes up to the present.

Taking in count the lasts 15 years we could notice how Brazilian economic growth has been linked to two different kind of economic measures. From the beginning of the XXI century to the peak of the financial crisis this growth was mostly due to hexogen factors, as a new and more intense commercial relations with countries with a similar stage of development, not only with the countries belonging in the Mercosur, signed in 1991 between Brazil, Argentina, Uruguay and Paraguay, but also countries of Asia, Africa and the Middle East. In addition the first mandate of Lula was also characterized by the will to fast the process of releasing Brazil from the dependency from European and US markets. From the 2007 financial crisis to the present Brazil started entrust more on its own force, rejecting the trend of being a container for foreign capital. As we saw in chapter two Brazil faced quite well the financial crisis that sharply affected it at the end of 2008, particularly the

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<sup>56</sup> IMF (2006).

<sup>57</sup> Central Bank of Brazil

industrial sector and saw a dramatic drop in the export of manufactured goods. Even though Brazilian economy started to recover in 2009, earlier than the rest of the world. 2010 has been the golden year of Brazilian economy: GDP grew of 7,5 points percentage<sup>58</sup>, domestic consumption became important for the economic growth, the Central Bank raised interest rates to keep foreign investment under control, demands of imported goods and services increased as a sign of the consolidation of the Brazil Economy recovery. In addition the government programmed to reduce its dependence on imported oil not only using bioethanol to substitute crude oil, but also with an internal production and gradual exportation of it after the discovery, in 2009, of enormous undersea oil deposits between Rio and Sao Paolo.

The lasts three years saw a slowdown of the Brazilian economic climb which calls the future of Brazilian economy into question. Looking at the positive things which support the ideas of those who see in Brazil one of the future's most powerful country, it is important to stress that Brazil is nowadays the seventh world power and in 2011 it surpassed United Kingdom gaining the sixth position. Thanks to its supremacy in exports of coffee, sugar, beef and soya Brazil could be defined as the *world's farm*. In addition the country is exporting crude oil since 2009, as we have already mentioned, and it is also the third bioethanol exporting country in the world. Furthermore in the lasts 5 years the volume of total exports doubled and even if imports at the same time grew by one and a half time, the overall balance of trade is in surplus.

Although these positive sign of growth are remarkable, they could not be taken as unreliable. In fact, as we noticed previously, Brazilian economy is sharply influenced by international markets volatility, in particular by that of China which is now passing through a moment of slowdown. Moreover Brazil does not seem able to take full advantages from its immense natural

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<sup>58</sup> IBGE (2011)

resources. In addition it appear hard to fix the serious structural deficiencies of Brazil, especially those concerning education, health, welfare, criminality, corruption and infrastructure. It remains much to be done: if the economic growth will be not followed by these important structural intervention, Brazil's development appears incomplete. These are warning signals that Brazil, but also the other BRIC's countries, could be entering a middle-income trap. The middle-income trap<sup>59</sup> is reached when developing economies grow quickly but struggle to maintain that growth because of a lack of structural reforms, labor market development and industrial growth.

To conclude, it could be said that Brazil is a high-potential country, with a huge human and natural capital. That is why Brazil could probably became one of the most powerful countries within 20 years. It is also true, as we have seen every time we dealt with economic measures, that Brazil is stuck in a short-run perspective. To avoid the middle-income trap Brazil needs to pass from this short-run viewpoint to a long-run one and unlock new drivers of economic growth. Otherwise the risk is that the country will stay forever in a limbo: Brazil is too small to be regarded with full rights as one of the world's biggest economic powers, but at the same time is too big to be considered a medium economic country. Brazil is growing under its possibilities, losing its chance to hop into a future which has yet to arrive.

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<sup>59</sup> As mentioned in David N. Weil, *Crescita economica*, Milano, Hoepli, 2007, p.57-73

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